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Department of Finance
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Ministère des Finances
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BUDGET SPEECH

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delivered by

the Honourable E. J. Benson

Minister of Finance

and

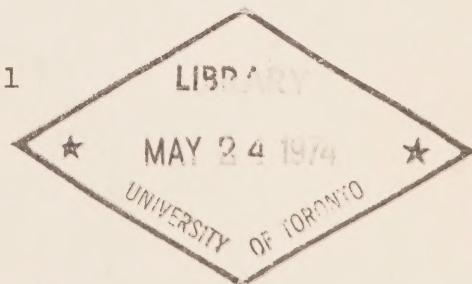
Member of Parliament for

Kingston and The Islands

in the

House of Commons

Friday, June 18, 1971





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Mr. Speaker:

This is an important and historic occasion. After almost a decade of study and public debate, we are now entering the final phase of the most comprehensive tax reform undertaken since the income tax system was begun in 1917. The legislation Parliament will be asked to approve this year will provide the framework for our income tax system for many years to come.

My budget presentation this evening will be somewhat longer than usual. This is because it is my intention not only to provide a broad outline of the tax reform we propose for Canada, but to discuss the economic situation and the fiscal policies appropriate in present circumstances.

The first step down the long road of tax reform was taken in 1962 by the former Conservative government. In response to a growing public demand for major revision of the tax system, the government of the day appointed the Royal Commission on Taxation, under the chairmanship of the late Kenneth Carter. In the spring of 1967, the commissioners published their report recommending sweeping changes in the system.

Shortly afterwards my predecessor as Minister of Finance, the Honourable Member for Eglinton, invited submissions from the public on the commission's report. Following a wide-spread public discussion the government tabled the White Paper on tax reform in November, 1969.

The government has considered the hundreds of submissions from organized groups in our society and the thousands of thoughtful letters from individual taxpayers.

The work of the two parliamentary committees was extremely important to the White Paper process. The members of the Commons Committee of Finance, Trade and Economic Affairs were able to assess not only the submissions from organized groups but as elected members of Parliament were able to assess public opinion among their constituents.

Both committees held lengthy hearings in Ottawa. The Commons committee also conducted hearings in provincial capitals.

The provinces, too, have put a great deal of time and effort into studying the federal proposals. For the first time they were invited to comment upon and criticize proposals for

changing the tax system and alternatives were put forward. After the White Paper was published, I met with provincial ministers many times on the subject of tax reform. It was also discussed at meetings of first ministers. Many of the provincial representations are reflected in the bill.

The White Paper process was an important step in the evolution of participatory democracy in Canada. Until now, it has been traditional for governments to implement tax policy by introducing legislation directly in this House. In this instance the government chose to adopt a different approach. This was done because the government believed that a fundamental reform of the existing tax system was necessary and that all Canadians should participate in the development of this reform. The government chose to express in a White Paper its view of what a tax system ought to be, and invited all Canadians and all levels of government to join in the discussion. As I have said many times, the White Paper reflected the government's view, but the government was not wedded to its proposals; rather, it was willing and ready to respond to suggestions for improvement, provided that the basic objectives of tax reform were maintained.

At the beginning of the debate, the government was able to participate openly in the dialogue. As the time for decision drew nearer, the traditions of budget secrecy forced us to limit more and more the public expressions of our views. However, throughout the entire process, we listened carefully to the constructive advice received from citizens, organizations and other levels of government.

The White Paper process was of great value. In the end, the federal government must assume its responsibility to recommend to Parliament the legislation which, in its judgment, will best serve the interest of Canadians. However, through the process of debate and discussion, it has been possible to develop a program of tax reform which not only meets the needs of Canada, but also reflects the views of Canadians.

The Goals of Reform

Mr. Speaker, the legislation I am introducing this evening represents a basic reform of our income tax system. To properly evaluate these proposals, it is important that we have a clear view of what a good tax system ought to be.

A tax system must be sensitive to the economic and social needs of this country. It must not stand in the way of steady and continuous growth and economic prosperity. In some cases, it must do more - it must stimulate sectors of our economy which need incentive.

A tax system must distribute the tax burden in an equitable manner, based upon ability to pay. Furthermore, it must not only be fair, it must be seen to be fair.

As stated in the White Paper, fairness in taxation implies two principles. First, it means that people in similar circumstances should accept similar shares of the tax load. Secondly, it means that people with higher incomes should be expected to pay in taxes a larger share of their incomes than persons with lower incomes.

To be acceptable to all citizens, a tax system must have as few loopholes as possible. Voluntary compliance cannot be maintained if it is apparent that special groups of taxpayers are able to avoid paying their fair share of the burden.

A good tax system must lend itself to efficient, economical and objective administration. It must be straightforward in both purpose and method, so that taxpayers know where they stand with a minimum of administrative discretion and litigation.

Finally, in the Canadian context, it is essential that the federal tax system be capable of being harmonized with provincial tax systems. This is necessary if we are to avoid a tax jungle.

I believe that the proposals which I will introduce this evening represent a reform of our tax system which will deal with many of its shortcomings. They will also reflect a consensus about what Canada's tax system ought to be in the 1970s.

Because this is a comprehensive reform, time will not permit me to discuss in detail the many individual changes proposed. So that members of this House will be able to obtain a clear understanding of what is proposed, the Notice of Ways and Means Motion which I will table tonight contains the full content of the tax reform bill. In addition, supporting documents provide a brief but comprehensive explanation and description of the various proposals.

It is my intention this evening to discuss the main features of the reform package, to explain its general direction and purpose and to review the revenue and economic implications.

The Thrust of the Changes

Mr. Speaker, I now want to describe the general thrust of our reform proposals and the manner in which they respond to the goals of a tax system and the needs of Canada.

First and foremost, by a combination of increased exemptions, changes in the rate schedule and other measures, we propose to reduce significantly the tax burden borne by lower-income Canadians. In recent years the combined effect of the income taxes, sales taxes and property taxes, of all levels of government, has put too heavy a load on those with the least ability to pay.

We propose a major reform of the definition of income so that our tax system will be more fair and equitable between taxpayers. As the most important element in this regard, we propose to tax capital gains. In addition, we propose to bring into the definition of income several other items which have not been taxed in the past. At the same time, we propose to recognize certain expenses as new deductions from income. The result of these measures will be to produce a better and fairer balance in determining the income that is brought to tax.

As part of this process, we will reform the tax treatment of wage earners -- the vast majority of our taxpaying population. We propose a number of measures which will more accurately reflect the changing composition of our labour force and the many expenses that this group faces in earning a living.

We propose a major reform of the tax treatment of corporations and their shareholders. This will eliminate much of the double tax burden at present imposed upon persons who invest through corporations.

In addition, the corporate tax system will give due recognition to the problems and contributions of small businesses -- a subject to which many Canadians attach a high importance.

We propose several valuable reforms of the administrative procedures. Our objective in this regard is to recognize in law the rights of taxpayers.

We propose a significant reform of the present treatment of our natural resource industries. We are fully aware of the importance of this sector of the economy. At the same time,

incentives in this area will be more directly responsive to the needs of this industry and to Canada's over-all policies in this area.

We propose important reforms for Canadians who carry on business abroad and non-residents who invest in Canada.

Finally, we have developed a program which will ensure that the increases in revenue derived from the more equitable distribution of the tax burden will be returned to all taxpayers. This program fulfills the government's commitment that tax reform will not be a stepping stone to tax increases.

Mr. Speaker, before I turn to a more detailed consideration of these reform proposals, a brief word on the timetable.

The tax bill will be introduced for first reading at the end of the budget debate. It is the government's intention that debate on second reading of the bill begin when the House reconvenes early in September. This will provide time for public study, and for the government to consider representations for technical changes. Meanwhile, we will discuss the legislation with provincial governments. I have asked for a meeting of finance ministers and treasurers in July. It is intended that the new system will come into effect on January 1, 1972.

Personal Income

The reforms with the greatest impact on most Canadians are, of course, those involving personal income. Low-income groups bear a disproportionate share of the tax load. Not only have the basic exemptions remained unchanged for more than 20 years, but provincial and federal sales taxes, which bear heavily on low-income groups, have increased substantially.

The legislation proposes to raise personal exemptions to \$1,500 from \$1,000 for single taxpayers and to \$2,850 from \$2,000 for married taxpayers. This substantial increase in exemptions, which goes beyond our original proposals, is the broadest and most fundamental move to provide tax relief.

Hundreds of thousands of elderly Canadians will receive further substantial tax relief through a combination of measures. The existing \$500 extra exemption for persons 70 years and over will be increased to \$650 and extended to all persons 65 years and over. The Guaranteed Income Supplement, which goes to pensioners with little or no income other than their Old Age Security pension, will no longer be taxable. Including the standard deduction, single taxpayers 65 years of age and over will be exempt on \$2,250 of income.

Blind persons and disabled persons confined to a bed or wheelchair will be given the same benefit.

Six out of seven Canadian taxpayers are the men and women of our labour force who earn wages and salaries.

A new employment expense allowance will permit wage and salary earners to deduct three per cent of employment income up to a maximum of \$150 a year. This measure will alleviate the cost of buying special clothes, or tools, or books required for a job, and put these workers on a more equal footing with the self-employed.

There will be a deduction of up to \$500 per child and up to \$2,000 per family for child care expenses. This will go a long way towards removing a deterrent that many women say prevents them from taking jobs. In some cases the deduction may be claimed by the father. Our estimates are that several hundred thousand families will benefit. In many cases genuine hardship will be relieved.

There will be broad deductions for the expenses involved in moving to a new job. These include the costs of transporting families and belongings, their meals and lodgings while moving, and the cost of cancelling leases or selling their residences. The changing nature of our labour force and our economy requires that Canadians have greater mobility if they are to accept job opportunities when they arise, and this measure is proposed with this in mind.

A related proposal is to make tax free to employees the benefits they receive from employers to cover transportation, board and lodging at distant work sites. This will be important to lumber and mining workers, drilling and exploration crews and employees at isolated bases.

Unemployment insurance premiums will now be deductible, while the benefits will be made taxable.

The list of deductible medical expenses will be expanded to include payments to a school for the care and training of mentally or physically handicapped persons or disabled persons. To keep pace with the development of more modern appliances and equipment to help handicapped or disabled persons, expansion of the list of deductible medical expenses will no longer have to wait on changes made only at budget time. The government will ask Parliament for authority to add to the list by Order-in-Council.

Medical expenses for which an individual has been reimbursed will not be tax-deductible. However, premiums paid to a non-government medical or hospital plan will be deductible.

The limit on charitable donations is increased to 20 per cent of the taxpayer's income from the existing limit of 10 per cent. Donations to registered national athletic associations which promote amateur athletics in Canada on a national basis will be eligible as charitable donations. Further, the government proposes a re-examination of this area to determine whether the traditional definition of charitable organizations is broad enough to reflect real need in the 1970s.

As part of the goal of defining income more fairly the bill proposes to make certain items taxable. These include:

- capital gains, which I will discuss later;
- manpower training allowances
- unemployment insurance benefits, and
- the value of medicare premiums paid for an employee by his employer.

They also include scholarships, fellowships and grants, but as suggested by the Commons Committee there will be a special \$500 exemption.

Averaging Provisions

The bill introduces two types of income averaging which are significantly more generous than the averaging provisions of the White Paper, and replace most of the special provisions under the present law.

The first is general income averaging which will be applied automatically by the Department of National Revenue when income in a year significantly increases over income in previous years.

The second type involves a system of forward averaging. This kind applies to capital gains, incomes of artists, musicians, actors and professional athletes and to lump-sum withdrawals from various kinds of retirement and profit-sharing plans. An individual who receives this kind of receipt in a particular year will be able to cushion the tax effect by purchasing an annuity to spread the income over a period of years.

Many people in our society are engaged in work that brings in a large income in some years and small incomes in other years. Without an averaging system, the progressive rate schedule deals unfairly with them.

At present farmers and fishermen are allowed to average their incomes every five years. This system is continued, but special provisions ensure there is no overlap with the new averaging provisions.

To avoid a retroactive change in the law, individuals making lump-sum withdrawals out of pension plans and profit-sharing plans may choose to use the existing formula for the portion of the withdrawal that relates to amounts accumulated up to the end of this year.

Retirement Plans

Mr. Speaker, one of the important changes will increase substantially the deductions for contributions to retirement plans. The limit for pension plans and deferred profit-sharing plans is increased to \$2,500 from \$1,500. In the case of a pension plan this means that a combined employee and employer contribution of up to \$5,000 may be deducted, compared with the present limit of \$3,000. In addition, the limit for deductible contributions to registered retirement savings plans is increased to \$4,000 (or 20 per cent of earned income) from \$2,500.

These changes will enable taxpayers to put aside considerably more money for their retirement and will also significantly increase the level of personal savings available to finance growing capital investment in Canada.

Another measure important to Canadian development provides that the foreign investments of pension plans, deferred profit-sharing plans and registered retirement savings plans may not exceed 10 per cent of their assets if they are to qualify for tax-free treatment. I am confident that these changes will have a significant effect in channelling the investments of retirement funds into Canadian development, which otherwise might well have been placed abroad.

At present there are few limitations on the investments that may be made by registered retirement savings plans. The bill introduces restrictions that are similar to those applicable to deferred profit-sharing plans.

Both of these new investment restrictions are effective this evening. They will not be applied retroactively. Investments now held may be retained even though they do not

qualify under the new rules. However new investments must meet the restrictions.

Mr. Speaker, as a result of all the changes in taxation of personal income that I am describing tonight, 1,000,000 taxpayers who would otherwise pay tax next year will be removed from the tax rolls. We estimate that taxes will be reduced for 4,700,000 taxpayers, and will be changed by less than 1 per cent for another 2,000,000 taxpayers.

All taxpayers who claim married status and whose income is from wages and salaries will pay less tax in 1972 than they do at the present time. Taxpayers filing as single whose income is from employment will pay less than at present on incomes of \$8,000 or less.

As I emphasized earlier, the \$650 deduction for taxpayers 65 years of age and over, together with the exemption for guaranteed income supplement payments, will also result in significant tax reductions.

Mr. Speaker, before concluding my remarks on personal income tax reforms, I would like to say a word about tax rates as the new system develops through the period 1972 to 1976. I have indicated that for the first year of the new system a high proportion of Canadian taxpayers will pay less than at present. I am pleased to inform the House that under the tax reform we shall be able to make progressive reductions in tax rates applying to all individual taxpayers during the years through to 1976.

In my opening remarks, I recalled the undertaking given to the Commons committee and confirmed many times since, that revenues produced under tax reform as such will not exceed the total that would be produced if the present system were to remain in effect. Through the maturing of capital gains taxation, the closing of loopholes, and the higher elasticity of revenues under the new system, substantial additional revenues would be generated as compared with the present system. Tax reform envisages that these additional revenues shall be returned to taxpayers.

If any changes are needed to meet new economic and social conditions, government will be required to justify them in seeking legislative authority from Parliament.

I am thus proposing a rate schedule in the tax reform legislation providing for progressive reductions in basic personal tax rates. This will be of increasing benefit to all Canadians, particularly those in the lower-income brackets. Specifically, the federal rate of 17 per cent on the first \$500 of taxable income will be reduced in each of the years 1973 through 1976 to reach a 6-per-cent rate at the end of that period.

Capital Gains

The most important reform to broaden the income tax base is the proposal to tax capital gains. At present Canadians in a position to earn significant amounts of their income through capital gains pay far less tax than other Canadians who receive their income from salary or wages. The debate on tax reform has demonstrated wide support for a capital gains tax.

The general rule will provide that one-half of capital gains will be included in income and taxed at ordinary rates. This, in effect, makes capital gains part of the progressive tax system, taxing gains according to ability to pay. One-half of capital losses will be deductible from taxable capital gains. Individuals may also deduct up to \$1,000 of deductible capital losses from their other income. Our system will be similar to that of the United States, which also includes half of capital gains in income.

The White Paper contained proposals designed to exclude most homes from taxation; but many taxpayers feared that their homes might still be subject to taxation. To eliminate this concern, there will be no gains tax on a taxpayer's principal residence.

While this proposal will adequately take care of personal residences, I have been concerned that it might impose hardship on farmers, particularly those with large acreage. Therefore, they will be able to choose either the exemption for residences I have just mentioned, or the exemption formula proposed in the White Paper.

For personal property, such as paintings or antiques, any item or set of items must have a value of at least \$1,000 before it could possibly be subject to a gains tax. This amount of \$1,000 is twice as high as that in our earlier proposals.

I cannot emphasize too strongly that to be subject to a capital gains tax an item of personal property first has to be worth more than \$1,000, second, must be the kind of item that increases rather than decreases in value over time, and third, apart from people who leave the country, a change of ownership must occur.

The introduction of a capital gains tax requires a starting point, so that only gains after that date will be subject to the new tax. Some time before January 1, 1972, a Valuation Day will be announced. Generally, capital gains or losses will be measured against the value of an asset on Valuation Day. This will ensure that gains accrued up to Valuation Day are not subject to tax.

In some cases, assets may be worth less on Valuation Day than their original cost. If capital gains were to be measured only from Valuation Day value, part of the amounts that would be subject to tax might merely be a recovery of cost. The bill will provide that in computing a capital gain, a taxpayer may use either the original cost, or the value of the asset on Valuation Day, whichever is higher. This will ensure that gains which are simply a recovery of cost are not taxed.

In computing a capital loss, a taxpayer will measure the loss against the lower of original cost or the value of the asset on Valuation Day.

Alternatively, taxpayers may simply elect to use Valuation Day value for all their assets.

The most important assets of Canadians will be completely free from capital gains tax. There will be no tax on personal homes or on personal property with a value of less than \$1,000.

There is no requirement to send any information to the government on Valuation Day. Towards the end of this year, the Department of National Revenue will publish an information booklet listing those items which might be subject to tax upon sale, and the type of records taxpayers would find useful to keep.

When a taxpayer leaves Canada, he will be considered to have disposed of all of his assets except those on which we will tax non-residents. The first \$5,000 of capital gains will be exempt.

Alternatively, a taxpayer may elect to defer any capital gains that are deemed to arise at the time of his departure, by agreeing to pay tax in Canada in the year in which he sells any of his taxable assets.

The bill will provide that the new capital gains tax system will apply to non-residents on the disposition of certain Canadian assets.

The rule relating to non-residents is, of course, subject to any existing treaties that Canada may have with other countries.

The bill will provide that, in a number of situations, a capital gain may be deferred. An important exemption from capital gains tax is the transfer of property between a husband and wife by gift or at death. They will not be taxed. The wife will simply take over the property at his cost and any subsequent gain or loss will be measured from that cost. Other situations include expropriations, certain business or corporate reorganizations, the incorporation of a proprietorship, the transfer of assets to a controlled corporation and amalgamations.

The White Paper proposed that shares in widely-held Canadian companies be revalued every five years. This proposal has been dropped. In its place, the government has adopted the recommendation of the Commons committee, several of the provinces and many taxpayers, to tax accrued gains when a taxpayer dies. The Commons committee also recommended that if this alternative was adopted, there should be a substantial reduction of death duties so that estates would not face the burden of two substantial taxes at the same time. When considering this issue, the government took into account that it receives only 25 per cent of the revenue from estate tax. We felt that an appropriate reduction would have to be of that order of magnitude to compensate for the new capital gains tax.

Accordingly, the government has decided to eliminate federal estate and gift taxes as of January 1, 1972.

Corporate Income

I come now to the provisions of the bill relating to the taxation of corporations and their shareholders.

The most important proposal concerns the basic corporation income tax rates. I referred earlier in my remarks to the fact that the tax reform system as it matures over the next five years will yield additional revenues compared with the present system. The basic corporation tax of 50 per cent at the outset of the new system in 1972 will therefore be progressively reduced in each of the years 1973 to 1976 by one percentage point, so that in 1976 the general rate will be 46 per cent.

This progressive reduction will bring the general corporate tax rate in Canada to a level below that in the United States, our most important trading partner and business competitor. Despite the many changes in our social and economic structure we must continue to look to the private sector and to business corporations to provide the jobs for our rapidly growing labour force and to produce the income required to finance our growing appetite for goods and services. I am confident that this major move to reduce substantially the general corporate tax rate will contribute in an important way to making Canada a most attractive place in which to invest, grow and prosper.

I turn now to some of the other important changes affecting corporations and their shareholders.

Small Business

This government supports the view that entrepreneurial initiative should be encouraged through the tax system. The Canadian economy depends upon the creative business activity of small, growing businesses.

The present low rate of corporate tax on part of the income of corporations is an inefficient method of encouraging the growth of small businesses. It is available to all corporations, regardless of their size. It is available regardless of the type of income they receive. It is available whether they are foreign-controlled or Canadian-controlled. It is available whether they are owned by large public corporations or by private individuals. And, it is available whether they are expanding or static enterprises.

However, with these deficiencies eliminated, a low rate can be an effective way of encouraging initiative by helping small corporations to accumulate capital for business expansion.

The corporate tax on the first \$50,000 of the business income of Canadian-controlled private corporations will be 25 per cent. This low rate will apply until a corporation has accumulated \$400,000 of taxable income under the new system. It will not be available to public corporations or to foreign-owned corporations or their subsidiaries.

If a corporation does not wish to expand its business in the year in which the small business incentive is earned, it can invest in short-term debt securities, or pay dividends to its shareholders. The dividends will, of course, be taxable in the shareholders' hands and, as a result, the income of the corporation will be taxed at the marginal rate of the recipients.

If a corporation employs the tax savings that result from the low rate for non-business purposes, such as portfolio investments, a special refundable tax will be imposed to recover the low-rate benefit.

We intend that the small business incentive be available only to Canadians and that it encourage Canadian ownership of our expanding businesses. Accordingly, if control is acquired by non-residents, the corporation must repay, over a five-year period, the tax saving it has received.

It had been my hope that a system might be developed to aid unincorporated as well as incorporated businesses. A great deal of time and effort has been spent towards achieving this goal both inside and outside government. Unfortunately, all the proposals were found to be unworkable. Accordingly, we reluctantly decided to restrict the small business incentive to incorporated business.

Double Taxation

Mr. Speaker, one of the problems of the present tax system is the double taxation of corporate income. One tax is imposed when the income is earned by the corporation, and a second when that income is distributed to the shareholders.

The White Paper proposed a comprehensive new system to deal with double taxation and to give Canadians an incentive to buy shares of Canadian corporations. Shareholders would have received credit against their personal taxes on dividends for the corporation tax paid.

This proposal became the subject of widespread controversy. Whatever its merits, the business community and a number of the provinces found it unacceptable.

It is for this reason that the government has decided to modify the existing system rather than to adopt the integrated system outlined in the White Paper. The modified system will retain and improve the present incentive to ordinary Canadians to invest in Canadian corporations.

This will be accomplished by increasing the rate of the dividend tax credit to 33-1/3 per cent of the dividend and requiring that the credit be included in income. This will remove the bias against lower-income shareholders by reducing the tax payable for those whose marginal rate is less than 40 per cent. The reformed dividend tax credit will offset in the hands of shareholders 25 points of corporate tax paid by Canadian corporations.

Since the low rate of corporation tax is restricted to business income, the investment income of private corporations will be subject to the normal rate of corporate tax. As a further measure to eliminate double taxation on these corporations, one half of the tax on investment income will be refunded when dividends are paid to shareholders.

Private corporations will also be able to distribute half of their capital gains tax-free.

The combined effect of these measures will substantially eliminate double taxation of the income of small private corporations.

As a result of these provisions, the taxation of investment income will be the same whether it is received directly or through a private corporation. Accordingly, it will no longer be necessary to have special provisions for personal corporations.

Mr. Speaker, I would like to mention briefly a few of the other important features of the new system.

- Dividends received by a private corporation from a subsidiary corporation will normally be tax-exempt, but dividends received on portfolio investments will be subject to a special refundable tax.
- Dividends received by public corporations from Canadian corporations will be exempt unless paid out of designated surplus.
- Corporations may distribute their earnings accumulated to the end of 1971 tax-free to their shareholders, upon payment of a 15-per-cent tax.

Business and Property Income

I wish now, Mr. Speaker, to deal with a number of important rules concerning business and property income.

At present Canadian corporations cannot deduct interest on money borrowed to buy shares in other corporations. This has undoubtedly put Canadian corporations at a disadvantage when competing in takeover bids with foreign corporations, which can deduct such interest in their home country. This feature of our tax system has been the subject of much criticism in recent years. The bill will permit Canadian corporations to deduct such interest. Assuming the full rate of corporate tax, this deduction means that the cost of borrowing money for this purpose will be cut in half.

Under the present tax system individuals can deduct interest on money borrowed to buy shares and this deduction continues in the new bill.

Currently a number of business expenditures, such as the cost of purchasing goodwill, are neither deductible as a business expense nor depreciable as a business asset. The bill will provide that one-half the cost of these items will be deductible over a period of time.

In a similar way, one-half of the proceeds from the sale of such assets will be included in income, with special rules to cover those owned at the start of the system.

During the debate of the White Paper the subject of entertainment and similar expenses was fully discussed. The consensus was that the present rules of the income tax system should be maintained, and that there should be no sweeping changes in this area. The new bill continues the present deduction for entertainment and related expenses, subject to several important changes to prevent deductions for expenses which are clearly personal.

No deduction will be permitted for membership fees or dues for clubs that exist primarily for the purpose of providing dining or recreation for members. Expenses related to a yacht, camp, lodge or golf course will no longer be deductible. Taxpayers may continue to deduct the costs of attending two conventions a year, but the conventions must be held within the area in which the association carries on its activities.

The new bill will continue the present system of capital cost allowance. However, there are three changes to remove some inequities in the present system.

First, losses created by capital cost allowances on rental property will not be deductible from non-rental income.

Secondly, each rental building costing \$50,000 or more that is acquired after 1971 will be placed in a separate capital cost allowance class.

Thirdly, when a taxpayer dies, he will be deemed to have disposed of depreciable property at an amount midway between its fair market value and its written-down value. This will provide treatment similar to the taxation of capital gains at death.

I would now like to turn to the provisions in the bill dealing with certain classes of taxpayers.

Farmers and fishermen will continue to compute their income on a cash basis and to average their income over five-year periods. Their special depreciation provisions and the basic herd provision for farmers will be phased out. Farmers will be given an opportunity to establish a basic herd and receive capital gains tax-free on their inventory at December 31, 1971.

The three-year tax-free period for co-operatives will be eliminated. They will continue to deduct patronage dividends. But this deduction may not reduce their income below five per cent of capital employed instead of three per cent as at present.

Caisse populaires and credit unions, which now are exempt from tax, will be taxed in a similar way.

The bill will provide that persons carrying on the practice of a profession must include amounts in income as fees are billed rather than as cash is received. This provision will bring the taxation of professionals more in line with the taxation of most other businessmen.

In general, the income of trusts will continue to be taxed as it is now. Income distributed to a beneficiary will be taxed in the beneficiary's hands. Income retained by the trust will be taxed in the hands of the trust.

When an estate is taxed on income that is retained the personal rate schedule will be used. Most other personal trusts in existence tonight will also use the personal rate schedule for investment income.

In general, personal trusts created after tonight will be taxed at the higher of 50 per cent or the personal rate schedule.

The taxation of partnership income will not differ significantly from the present treatment. Partners will continue to be taxed on their share of the partnership income as if they had received it directly, although the computation of income will be made at the partnership level. As a result of this method of computing income, capital cost allowance will be taken by the partnership rather than by the partners.

Mining and Petroleum

In devising a tax system for the mining and petroleum industries that will best serve the national interest, it is essential to reach a balanced judgment on their role in the development of slow-growth regions, the present and prospective worldwide demand and supply, the risk involved in these industries, the international competition for capital, and the levels of incentives available in other countries.

It is the government's intention to continue tax incentives at a reasonable level for these industries. At the same time we want profitable projects to bear a fair share of taxation.

The bill will introduce a system that is basically the same as the White Paper system, modified by my announcements of last August.

The three-year exemption for new mines will be withdrawn at the end of 1973. In place of this incentive, assets related to a new mine will be eligible for accelerated depreciation. The cost of these assets may be written off against income from a new mine as quickly as the income will permit. Social capital related to a new mine, such as houses, townsite facilities, schools and hospitals, will all be eligible for this fast write-off.

The next major change for mining and petroleum income is that the present automatic depletion deduction will end in 1976. After that, depletion will be earned. Every \$3 of eligible expenditure will earn \$1 of depletion. Eligible expenditure will be exploration and development costs, the cost of most new mine assets which qualify for fast write-off and certain new processing facilities and expenditures connected with major expansions of a mine. Eligible expenditures made between November 7, 1969, and December 31, 1976, will earn depletion for 1977 and subsequent years.

The five-year delay in introducing the earned depletion system should give mining and petroleum corporations a reasonable time period to adjust to the new system. The present automatic 25-per-cent depletion deduction allowed to non-operators will be continued until 1976. In 1977 it will increase to 33 1/3 per cent, but it will have to be earned.

After 1971 the depletion allowance given to shareholders of mining and petroleum corporations will be withdrawn.

The bill will also implement the proposal made in August to provide a federal abatement of 15 percentage points for provincial mining taxes, beginning in 1977.

International Income

Mr. Speaker, I turn now to the taxation of international income.

Most of the proposed changes in this area will not take effect until 1976. This will allow a reasonable period of time to renegotiate existing treaties and to negotiate new tax treaties, especially with developing countries. In their treaties, many foreign countries give significant tax concessions to corporations of other countries. If Canadians and Canadian corporations are to be competitive internationally, we must win for them these same concessions.

In all treaties, we will be prepared to exempt dividends received by Canadian corporations out of profits earned in the foreign country by a corporation in which the Canadian has a substantial interest. In exchange, we will expect the foreign government to extend to Canadians the same tax concessions they grant to other foreigners.

After 1975 dividends received by Canadians from affiliated corporations in non-treaty countries will be wholly or partly exempt in Canada, depending on the level of foreign taxes paid.

In order not to discourage investment by Canadians while treaties are being negotiated, special provisions will cushion Canadians against this tax effect.

A number of foreign countries impose taxes substantially lower than those in Canada, and investment income has been diverted to these countries to avoid Canadian tax. Rules starting in 1973 will tax the investment income of foreign affiliates to the same extent as if it had been received in Canada.

Unless it is reduced by tax treaty, the general rate of Canadian withholding tax on investment income paid to non-residents will be increased to 25 per cent in 1976.

New foreign tax credit provisions improve the position of Canadians now facing double taxation on their foreign income.

Pension and similar payments after 1971 to non-residents will be subject to withholding tax. However, no withholding tax will apply to the Old Age Security pension of \$960 and to \$1,290 of the Canada or Quebec Pension Plan payments. This exemption is equal to the amount exempted for single Canadians 65 years of age and over. In the few cases where the withholding tax is more than the tax that pensioners would pay in Canada, they may file Canadian returns and obtain refunds.

Appeals, Administration and Civil Rights

Mr. Speaker, I would now like to refer to changes which the government is proposing in the appeal, administration and enforcement provisions of the Income Tax Act. I am confident that these proposals will be welcomed by all members of this House.

It is important that the review and appeal procedures under the act permit disputes to be resolved quickly, efficiently and at minimum cost.

In recent years, administrative review procedures have been substantially revised to accomplish this end. We now propose to improve the judicial appeal procedures to permit faster and easier access to the courts.

If National Revenue denies or revokes registration of a charitable organization, amateur athletic association, retirement savings plan or profit-sharing plan, a taxpayer may henceforth appeal to the courts.

At present the Minister may issue a reassessment of an income tax return more than four years after filing where there has been misrepresentation or fraud. If the reassessment is issued, it may extend to matters not related to the fraud. The bill provides that this reassessment may not extend beyond the original matter in question.

Changes will also be proposed in the procedures followed in inquiries held under the authority of the act. The Tax Review Board will appoint a hearing officer who will preside over such inquiries and exercise many of the powers provided for in the Inquiries Act. The right of witnesses to be accompanied by counsel and of persons whose affairs are being investigated to be present or represented throughout the proceedings will also be specifically provided.

Many of the changes I have just outlined result from suggestions put forward by the Canadian Bar Association and the Canadian Institute of Chartered Accountants. I would like to thank these organizations for their assistance.

Mr. Speaker, I feel that these and other changes will help to simplify many of the administration and appeal procedures of the Income Tax Act and will further confirm and protect the civil rights of taxpayers under the act.

Provincial Taxes

The federal government is prepared to continue to collect provincial income taxes without cost to the provinces. This system has proven its worth to the provinces and to taxpayers, and we would hope that most provinces will wish these arrangements to be maintained. The unified collection system involves agreement by the provinces to define their personal income tax as a percentage of the federal tax and, therefore, to adhere to the same rules for determining taxable income and the level of exemptions. The provincial rate is determined by provincial legislatures specifying the percentage to apply to the federal tax. In the case of the corporate tax, provinces levy their rate upon taxable corporate income as determined by the federal act.

The present federal personal tax, upon which agreeing provinces specify their rates, contains a general abatement of 28 per cent applicable to all provinces. The general abatement system will be discontinued beginning next year, as proposed in the White Paper. At the same time, the old age security tax, the social development tax and the 1966 tax reduction have been integrated with the general rate structure, and the temporary surtax has been eliminated. The net result of these changes is to reduce the size of the federal tax which is the base to which provincial rates are applied. This will require provinces to express their nominal tax rates on a slightly higher basis to derive the same dollar revenue. These higher rates will not, of course, mean higher taxes for provincial taxpayers. They arise only as a consequence of expressing tax rates on a smaller base. The precise provincial rates that will yield the same tax revenues for provinces as they now get, will be discussed with the provinces shortly.

The White Paper made an important revenue commitment to provincial governments. That guarantee stated that provinces which continued to have their taxes collected by the federal government under rules in harmony with ours would be protected against unforeseen reductions in the combined yield of their personal and corporate income taxes for several years. The federal government will fulfil this pledge by payments to provincial governments, if required, for the years 1972 to 1974. The guarantee will take into account the requirement to increase the nominal provincial rates as I have just explained.

Economic Effects of Tax Reform

I should like now, Mr. Speaker, to discuss the implications of these tax proposals for foreign ownership of Canadian industry, for savings, investment and growth in the Canadian economy and for the balance of payments.

Several features of the proposals will increase the attractions to Canadians relative to non-residents to acquire equity in Canadian enterprise. First, Canadian corporations will be permitted to deduct as an expense, interest on funds borrowed to finance the purchase of shares in other corporations. This measure will eliminate a disadvantage which Canadian corporations have had in competing with foreign corporations in take-over bids. Second, the ten per cent limitation on foreign assets of pension funds and retirement savings plans will have an important influence in channelling the funds of these large intermediaries to Canadian businesses. Third, the lower tax rate for small

business will be available only to Canadian-owned companies and tax savings afforded by this incentive will be recoverable should the ownership of companies which have benefited from them pass to non-residents. Finally, the form of the dividend tax credit makes the incentive to invest in shares of Canadian corporations even more attractive than it has been for most Canadians.

In assessing the other economic effects of the reform measures, it is extremely important to bear in mind that the amount of revenue generated by the new system will not exceed that of the present system less the personal and corporate surtaxes. There will be no adverse effects of the kind that would occur if there were an increase in the overall tax burden. The effect instead is that the existing burden will be redistributed in such a way as to improve the equity of the system and to make it more neutral in its treatment of different types of income. These are important improvements and I would emphasize that it has not been necessary to purchase them at the expense of economic growth. Let me develop this point.

Under the new tax system most Canadians who derive their income primarily from wages and salaries will pay lower taxes than they now pay. This improvement in personal disposable income will raise the demand for goods as well as personal saving. The measures which benefit working mothers will have the effect of making it easier for them to join or remain in the labour force if they wish. The progressively declining corporate rate will contribute to higher corporate savings and investment. The new tax system will continue to provide reasonable incentives to the mining and petroleum industries and I see every reason therefore to anticipate their continued rapid growth.

The taxation of capital gains will of itself reduce somewhat the capacity, particularly of higher-income Canadians, to save and will affect adversely also the savings of corporations having taxable capital gains. There may be some adverse effects on the saving of mining and petroleum companies. We have, however, provided substantial offsets to these adverse effects. This has been done by removing the federal estate and gift taxes, by granting more generous treatment of contributions to pension and retirement savings plans, by reducing the taxes of many persons, by removing more than 20 percentage points from the highest personal tax rate, by lowering the general corporate rate progressively to 46 per cent and by offering improved provisions for averaging of income for tax purposes. I am confident that the combined effect of these measures will cause the net impact of the new tax system upon savings to be minimal.

On the balance of payments, the net effects of the new measures will also be negligible. Several of the individual measures will have effects on particular items, but they will not all be in the same direction and I do not expect any significant overall effect.

I should like to conclude these remarks on the economic effects of the reform measures by restating my conviction that in achieving greater equity it has not been necessary to sacrifice growth. Our potential and prospects for economic expansion are undiminished.

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Economic and Financial Position

Mr. Speaker, I turn now from the tax reform measures to review our economic and financial position and to propose certain measures which will further contribute to our economic expansion. I realize that honourable members have already listened to the equivalent of a full length budget speech and so I shall be as brief as possible. A Minister of Finance must speak of taxes, but in doing so I do not wish to tax the indulgence of the House. Members will have available the Budget Papers that I tabled Wednesday.

In my budget speech of last December I said:

"We are looking to growing increases in the value of gross national product next year, which by the second half may be running at a rate about 8-1/2 per cent above the second half of this year. With continued good price performance these figures imply an increase in real output that will be sufficient to more than offset the increase in the labour force and expected growth of productivity and so reduce unemployment progressively during the year."

Tonight, some six months later, this is still my general view of 1971. In fact, my view of the advance of the economy in the second half of this year is even stronger than it was last December. I expect that the gross national product for the balance of this year will be 9 per cent or more above the same period last year.

The Canadian economy last autumn marked a turning point from declining to expanding rates of growth in demand, output and employment. I am confident that as we move on through the second half of 1971 and into 1972, the performance of the economy will be strong and gaining momentum.

This is my assessment of the economic situation. I would like to go into more detail, however, and in doing so to indicate not only features that inspire and reinforce my confidence but also some that are cause for concern.

The results for the fourth quarter of last year and the first quarter of this year have been distorted by the consequences of major strikes. Therefore, to gain perspective let us compare results for the fall and winter combined, with

those for the previous spring and summer. After this view in perspective we may look at the first quarter of this year in more detail and at developments since then.

In the spring and summer of 1970 the value of GNP, apart from price changes, was growing at an annual rate of only 2.2 per cent; but in the subsequent fall and winter real output grew almost twice as rapidly. This is one way of revealing the turnaround in activity of which I have been speaking. Important strengths and weaknesses in the situation may be seen by comparing the developments of the main categories of total demand. Last spring and summer, consumer expenditure grew at only 0.9 per cent; in the fall and winter it was growing at 5.7 per cent. Investment in housing, which was declining rather precipitously last spring and summer, grew at an annual rate of just over 30 per cent in the fall and winter under the stimulus of federal government financing. Government expenditure in both periods increased at rates very much in excess of the rate of growth of real GNP and was an important factor in sustaining and stimulating the economy. The balance of our international transactions in goods and services moved sharply into surplus last spring and summer. Despite this remarkable gain in our trading position, the gain in the subsequent six months more than doubled that performance. The weaker parts of the economy were in private capital investment in commercial and industrial buildings, machinery, equipment and inventories.

Employment, which grew by 140,000 jobs last spring and summer, grew by 180,000 in the fall and winter. This increase was not sufficient to bring the unemployment rate down far enough.

Looking at price developments in the same way, consumer prices seasonally adjusted were rising at a rate of 2.6 per cent during the spring and summer last year. By last fall and winter this rate of increase had been cut almost in half.

This, then, is the view of our economic developments in perspective. It is a view of an economy embarked on expansion with moderating price increases. But it is an economy in which unemployment remains too high and business investment has not yet begun to respond and contribute to the advance.

The First Quarter 1971

Let us now look at the data for the first three months of this year, although as always it is harder to bring recent

information into focus. The first quarter national accounts gave an unclear and inconclusive picture. The Bureau of Statistics announced when it released these figures that it would be making upward revisions in them. I will deal with the figures as they stand.

What the figures show is that total domestic demand, apart from price changes, increased in the first quarter at the very high annual rate of almost 8 per cent. Housing was a strong component. As the recent very high levels of housing starts turn into high levels of completions later this year not only will investment in housing remain high, but spending for home furnishings will also rise. Indeed, consumer spending for durable goods is already up sharply this year. Auto sales following the auto strike, of course, contributed to this increase.

Expenditures by all levels of government were high in the first quarter and judging from the budgets presented to provincial legislatures this spring will remain high throughout this year.

Business spending on buildings and on machinery continues to be the weakest element in the economy. There is no surprise in this, although some gains are expected in the second half. Business profits have been very badly hit by the stiff jumps in costs that have continued greatly to outstrip productivity growth. No doubt also an atmosphere of unusual uncertainty deriving from the continually rising costs, from last year's sluggish demand and from concern about tax reform has had a constraining effect upon business investment. I have dispelled some of that uncertainty tonight. Moreover, profits have now turned upward. Counting in the increases stemming from resumed car production, they are reckoned in the national accounts to have increased by over 10 per cent in the first quarter. Finally, as I have said, total demand is now advancing strongly.

So the stage is being set by reviving profits, growing demand and greater certainly for improved business confidence and increased capital investment this year and next.

Consumer buying of all goods and services other than durables has been relatively slow so far this year. But here, too, the stage is being set for advance. Personal savings continue to be high and consumer credit is readily available. As consumers, financed with high savings and credit, spend more, productive capacity will be more fully utilized, capital investment will grow, more jobs will be created and more income earned to support yet higher levels of spending.

The figures of exports and imports in the first quarter are very greatly affected by the swings in automobile exports and imports occasioned by the strike. The same is true of the business inventory figures. It is simply too early to be certain how to read these figures in relation to the strike effects.

In summary, the national accounts for the first quarter showed a very strong surge in domestic demand in spite of continued weakness of business capital investment. As for employment, the first quarter data show a strong increase of 1.2 per cent in the number of jobs. This was the highest quarterly rate of increase for two years. Clearly, then, the economy continued to move forward in the first quarter.

The information that has come in since the end of the first quarter confirms that the economy is gathering strength. The least satisfactory figures were for industrial production and unemployment in April. The retail sales figures for April, published this week, show their strongest monthly advance of the year. This is true of the sales of motor vehicle dealers, but it is also true of all other retail sales. Manufacturers' new orders and shipments which showed some hesitation in March were moving forward vigorously again in April. An unbroken rise in unfilled orders foretells sustained and rising manufacturing output in the future. The value of building permits issued for non-residential construction for the first four months of this year is more than 5 1/2 per cent above that of the same period of a year ago. Housing starts continue to be high. Exports in May were up, seasonally adjusted, almost 5 per cent over April, and some 4.7 per cent over the very high figures of a year ago.

Prices and Costs

Canada had a good record of price performance in 1970 - a record better than that of any other industrial country. The consumer price index increased by 1 1/2 per cent over the year from December, 1969, to December, 1970, and over the last half of the year there was virtually no change in the index at all. During the summer and fall of last year a very substantial decline in food prices contributed to our good record. So far this year there has been a renewed advance of food prices which has not yet offset last year's decline, but the increases in the group of items other than food continue to moderate.

While we may take satisfaction from the relief that the slower advance in prices has afforded, the continued rise of costs does not permit us to be sanguine about future price movements. There has recently been some modest abatement of cost increases. But in spite of this modest abatement there continues to be an upward push on unit costs of production. This has been tempered somewhat by the rise in productivity we have been experiencing. Such productivity increases are normal in the early stages of an economic expansion. We may welcome the effects of higher productivity on costs and prices and in guarding the competitiveness of our industry, but we must recognize that a reluctance to expand employment is the counterpart of industry's quest for greater productivity in this early phase of the new expansion.

The U.S. Economy

The performance of the Canadian economy has been rather different from that of our American neighbours. Of course there are, as always, broad similarities. But over the past year or so the major changes in the economic tempo have been rather less extreme here. The percentage rate of inflation reached a higher peak in the United States than in Canada. The falling off in the rate of growth of output was distinctly sharper in the United States. Indeed, the real value of output declined in the United States last year while in Canada it rose by some 3.3 per cent. Average unemployment rose more sharply in the United States in 1970 than in Canada. A basically declining trend in unemployment began here in the third quarter of last year, but a comparable turnaround has not yet appeared in the United States. All of these data suggest that while we cannot insulate ourselves from the pervasive impact of economic influences from the United States, we have it in our hands to achieve a somewhat better performance if we have the wisdom and the will to do so.

Balance of Payments

The declining trend in the U.S. economy last year had a marked effect on the destination of our exports. Our exports to the United States increased only moderately and the share of our exports to that country declined to 65 per cent from 70 per cent the year before. Very considerable increases occurred in the volume and shares of our exports going to Europe and to Japan. While our exports of merchandise showed quite

fantastic strength last year, imports fell over much of the year and consequently our merchandise account moved to the unprecedented surplus figure of \$3 billion. This strong merchandise trade position has continued into the first quarter of this year in spite of the rise in imports which occurred in the first three months.

The services or non-merchandise part of our international accounts which is typically in deficit, provided some offset to the growing trade surplus. Nonetheless the combined figure, for all current account transactions, was a surplus of some \$1.3 billion, a swing of over \$2 billion from the more typical deficit of the previous year. This strong overall current account position has continued into the first quarter of this year.

The changes in the capital account of the balance of payments have been equally striking in recent quarters. Net inflows of long-term capital fell off very sharply. Many factors contributed, such as the narrowing differential between long-term interest rates in Canada and abroad and my own request to borrowers to explore fully the possibilities of obtaining financing in Canada before offering securities abroad. My purpose in making this request was to assist the adjustment of the capital account to the vastly changed current account situation and so relieve the upward pressure on the value of the Canadian dollar. I want to record my appreciation of the excellent cooperation we have been receiving from most quarters in this regard, and to suggest again that their continued cooperation along these lines can do much to reinforce the attack upon unemployment in the period ahead.

As I mentioned, a combination of factors reduced the level of long-term capital inflow. The outflow of short-term capital was also lower in 1970. The net result of all capital movements was an inflow of just short of a quarter of a billion dollars. This capital inflow combined with the extraordinary current account surplus of \$1.3 billion to produce an increase of reserves of rather more than \$1.5 billion.

Most of this increase in reserves was accumulated, or committed through forward contracts, before the decision in May, 1970, to allow the value of the dollar to float. After that decision the pressures in the market appreciated the value of the Canadian dollar by about 6 per cent up to the end of the year. Since then the value of the Canadian dollar has declined somewhat. I welcome this development.

I have said on many occasions that the government did not wish to see the Canadian dollar appreciate. A higher dollar works with increasing effect against our exporters and against domestic producers who must try to meet foreign competition. Since the appreciation affects the economy in this way; it works against our policy of trying to expand employment opportunities in Canada. The government is very conscious of the impact of the higher value of the Canadian dollar on Canadian producers.

Recent Developments in Economic Policy

The monetary policy pursued by the Bank of Canada has continued to give support to the broad economic objectives of the government. For over a year it has been expansionary in character. The consequence of this policy has been to increase the liquidity of the economy considerably and to reduce interest rates. These reductions have been most notable in securities of shorter maturity, but mortgage rates and long-term bond rates have also declined. This setting of monetary policy has been desirable, not only to provide a suitable financial climate for stimulating the economic expansion but also for assisting in the adjustment of our international capital flows in order to avoid undue appreciation of the Canadian dollar.

It is not only the monetary policy which has been providing stimulus to the economy. The government set in train a series of expansionary expenditure moves with the budget of March, 1970. These were followed with additional expenditure measures in June, in August, in October and in my December budget. These measures, taken together, added upwards of \$900 million in fiscal stimulus to the economy.

In making decisions on expenditures we have had to choose carefully from among all the many competing demands for increased public spending, but during the past and current fiscal years, expenditure increases have been mainly directed to three broad and important areas: first, to help the provinces; second, to finance major initiatives in the field of social security; and third, to provide further measures for strengthening the structure of the national economy. All of these efforts have been designed to assist the growth, stability and welfare of our country. As such they are integral parts of a co-ordinated economic and social policy.

As regards the provinces, it is interesting to observe the basic support now being provided to provincial budgets by federal equalization grants. This year they will total just over

\$1 billion, up from \$370 million five years ago when the present fiscal arrangements were made. Apart from their rapid growth, these grants have also helped greatly in stabilizing provincial revenues during the recent period of slower growth. In addition, the special steps to accelerate payments of tax collection receipts and capital grants for technical schools provided over \$300 million for increased provincial spending. The special development loan program of \$160 million has also been well received. All but two of the provinces have claimed the full amount of their allocations for financing accelerated capital development projects to be undertaken by the end of the fiscal year. Saskatchewan has notified us that it does not intend to avail itself of its share; Ontario has indicated its wish to make use of this fund, but has not yet taken up its allocation.

More broadly, I might note the increasing interaction of federal and provincial public finance. This year over \$4 billion of federal budgetary resources - more than 31 per cent of the total - will flow to support provincial-municipal services. Only five years ago the comparable percentage was not quite 23 per cent. In July I will be meeting with provincial finance ministers to examine tax reform once again, and to discuss the renewal of the Federal-Provincial Fiscal Arrangements Act. As on previous occasions, we will be grappling with complex issues and conflicting pressures. I am sure, however, that our common aim will be to try to work toward a system of fiscal federalism that best serves our contemporary needs.

In the area of social security, the increase in the guaranteed income supplement for the needy aged went into effect April 1. That increase adds almost \$200 million in improved benefits for this group this year. At the other end of the age ladder, the proposals on restructured family allowances will have a further re-distributive effect. The major transformation in unemployment insurance - widening coverage and extending and increasing benefits - builds a firmer foundation of income support for virtually all Canadian wage and salary earners. As of this year, medicare is now operative in all ten provinces. Regardless of its birth pangs, that system involving \$550 million in federal grants to the provinces now assures every Canadian, regardless of his income, of the right to basic medical services.

All of these measures - each a major step in itself - contribute in a real and selective way to the same goals of equity and justice which we have sought to achieve in tax reform. They build in, as well, stronger safeguards against periodic slowdowns in the growth of the total volume of demand, and thus add new dimensions to the automatic stabilization of the economy.

In the area of measures for strengthening the structure of the national economy, we have been concerned to integrate the short-term stimulus in spending with longer-term structural needs. A major point of emphasis has been to increase the attractions to industry to make investments in the slow-growth regions. This has been centred mainly, but by no means exclusively, in the industrial development programs of the Department of Regional Economic Expansion. A large part of these outlays are incentive grants to increase the productive capacity of the private sector. This development thrust has recently been bolstered by the designation of a major new region eligible for incentives and the new loan guarantee provisions added to the Regional Development Incentives Act. The special program to assist the shipbuilding industry announced only last December has also been quickly and remarkably effective. The new orders from France announced last week by my colleague, the Minister of Industry, Trade and Commerce, already have pushed the total value of work to be undertaken by Canadian shipyards under the program to some \$250 million.

For the prairie region, we have provided - this year and last - a total of \$185 million in direct aid to assist its basic agricultural industry. At the same time we are trying to provide for a new, long-term approach to stabilizing the incomes of prairie farmers. In the north, a stepped-up program of investment in the development of both human and natural resources, and in the protection of its fragile ecology, is well under way.

New initiatives and new investments are well advanced on important fronts - in transportation services, including new airports and the experimental program for short take-off and landing air services, in defining an appropriate federal role and contribution to the orderly development of major cities, and in bringing adequate federal resources to bear upon the problems of pollution and of the environment. All of these programs are of special relevance to our rapidly-expanding metropolitan regions, where sustained and stable growth is of such importance to us all.

These measures taken together with the monetary policy are imparting a major stimulus to the economy. The full impact of this stimulus has yet to be felt, for the effects of policy action take time to build up. We can, accordingly, count on continuing impetus from the policies already in place. In addition, as I have explained earlier, the income tax system that I have proposed tonight, to come into effect at the first of January, 1972, will take some \$320 million less out of the economy than the present tax system. Corporations and millions of taxpayers will pay lower taxes than they are now paying. Not only that, but it will be a fairer system and one which will

protect and enhance incentives to invest and to work. We may, therefore, count on the tax reform measures to add to the fiscal stimulus of the economy.

Budget Measures

As Minister of Finance, I have explained many times the view of this government that fiscal policy is not a once-a-year affair. Our record is that of a government that adjusts its fiscal stance to the requirements of a changing economy and not according to a rigid calendar. In keeping with this record Mr. Speaker, I have further measures to recommend to the House now that will supplement those already adopted and whose effects are still being realized. The government is determined to do what governments can do to ensure that the expansion in real income and employment now under way shall be vigorous and broadly based. The building up of such an expansion depends ultimately on the decisions of the millions of persons and of the thousands of businesses that make up the private sector of the economy. To achieve the results we seek, these decisions of investors and consumers cannot be defensive and protective; they must be bold and confident decisions. The principal measures I have to propose are designed to encourage this kind of confident spending in the private sector of the economy.

Income Taxes

I propose first, Mr. Speaker, that effective July 1 the 3-per-cent surcharge on personal incomes be removed. This measure alone will add \$90 million to the buying power available to Canadian families and individuals between July 1 and the end of this year. The tax reform reduction that I outlined earlier tonight will continue this particular increase in consumer buying power into 1972 at an annual rate of \$210 million.

Beyond this, I propose to change the lowest rates of federal tax to eliminate taxes after July 1 on persons with taxable income of less than \$500. This immediate measure anticipates introduction of the new system with its benefits for taxpayers of lowest incomes. For example, a married taxpayer with two children will pay no further tax this year on employment income up to \$3,200. The rate changes will also provide some tax relief between July and January for all taxpayers with taxable income under \$3,000.

I also propose to assist pensioners with the lowest incomes. It is unfortunately true under our present rules that

some of our most needy pensioners pay tax on part of the guaranteed income supplement they receive. I propose to exempt the supplement from tax, retroactively to January 1, 1971. In this I am again bringing forward a feature of the tax reform. The consequent tax saving will be very welcome to the needy pensioners who will benefit.

These last two changes mean an end of income taxes for more than three-quarters of a million taxpayers as of July 1.

I estimate that in the current fiscal year the cost in revenue of all of these measures respecting the personal income tax will be in the order of \$135 million.

Mr. Speaker, I want now to refer to corporation taxes and to propose an immediate change affecting all tax-paying corporations. The 3-per-cent federal surtax on corporation income tax will be withdrawn effective July 1. This measure will leave about \$40 million in corporate hands this year. There will be no surtax under tax reform; thus, this particular advantage will also be a continuing one.

Sales and Excise Taxes

I have three important commodity tax reductions to propose tonight.

A sales tax on an important item of food has remained in our tax system too long. I refer to the 12-per-cent sales tax on margarine. I am pleased to announce its immediate withdrawal. This exemption will also cover other similar spreads sold under brand names. This tax is between two cents and four cents per pound, depending on the product, and its removal will reduce revenues for a full year by about \$7 million. The industry has promised to pass on the tax savings and therefore the grocery bill of Canadians should be reduced by at least this amount.

To further encourage the acquisition of anti-pollution equipment, I wish to announce the immediate withdrawal of the sales tax on such equipment used in production. This new exemption will apply to all machinery and apparatus which manufacturers or producers acquire to detect, prevent, remove or reduce pollutants of water, soil or air. The exemption will reduce revenues by about \$8 million a year.

The 15-per-cent excise tax on home entertainment equipment such as hi-fi's, radios and television sets and certain other electronic items is particularly onerous for an important secondary manufacturing industry which is at a disadvantage relative to foreign competition in respect of this tax. This action will reduce significantly the prices of these items.

For example, on a major item such as a \$500 television set, the retail price should come down by at least \$75. The reduction in revenues in a full year will be about \$40 million.

Impact of Tax Measures

This group of measures, added to those we have implemented over the last year will, I am confident, provide any extra insurance that may be needed against the emergence of a pause in the expansion that got under way last fall. They are directed specifically to the encouragement of the spending and investment in the private sector at large which is so necessary to sustain an expansion of employment and income. The reduction of personal income taxes will make a quick and material contribution to the growth of consumer spending. The reduction of corporate taxes will give that sector added encouragement to make new investments and thus to gear for and contribute to the growth of demand. The reduction in commodity taxes will also have an important stimulating effect. All of these changes taken together with reductions in income taxes provided for in the tax reform, will give us an adjusted tax system that will provide a sure and firm foundation for confident decisions in the private sector of the economy.

Customs Tariff

I should like to propose now a number of amendments to the Customs Tariff designed primarily to improve the competitive position of important Canadian industries. Like tariff changes in previous budgets they are to come into effect tomorrow. Several of the important changes stem from two Tariff Board reports relating to the Canadian petrochemical industry. One is concerned with the duty on petroleum fractions used as feedstocks in making certain chemicals. The cost of feedstocks represents a significant element in the cost of making petrochemicals in Canada. The board recommended that the present rates of 3/4 cent per gallon under the British Preferential Tariff and 1 cent per gallon under the Most-Favoured-Nation Tariff be reduced to 1/3 cent per gallon and this is the rate which I propose be implemented.

The second report involves the duty on polyethylene. Honourable members will recall that in my budget of October 22, 1968, I introduced a new schedule of tariff items for chemicals and plastics; the schedule was based on a Tariff Board study covering this important sector of the Tariff. For synthetic resins the board proposed a duty of 10 per cent on most of the resins made in Canada. However, for polyethylene resins the board decided that the rate of 7 1/2 per cent should remain unchanged. I asked the board to further review the duty on this product. In light of more recent information, the board recommended a 2 1/2-percentage-point increase in the duty on polyethylene resin with corresponding increases in duty on further processed forms of polyethylene, bringing these rates into line

with those on other Canadian-made plastics. These new rates do not require any renegotiations under the General Agreement on Tariffs and Trade because they are the rates agreed to in the Kennedy Round. I am sure that the Canadian chemical industry will view the action taken on these two reports as a sign of the government's continuing interest in its healthy development.

As a result of the Kennedy Round a new tariff system was introduced for production machinery. A key feature of this machinery program was the provision for free entry for such machinery when it is in the public interest and when the machinery is not available in Canada. This program has been most successful in that it has ensured moderate protection to the Canadian machinery industry and at the same time assisted Canadian firms to reduce the costs of acquiring such capital equipment as must be imported. We have been reviewing the scope of this program and I am now proposing to extend it to machinery used in sawmills and logging, as a measure of assistance to the forest industry.

I have received representations from various interests - particularly from the pulp and paper producers and from utility organizations in the Atlantic provinces - expressing concern about the supply and price of heavy fuel oils. Prices have risen substantially in recent months. I am therefore proposing that the 1/3-cent-per-gallon duty on such oils be set aside for a two-year period. This will relieve the pulp and paper industry alone of over \$3.5 million in costs.

These important changes in the Customs Tariff which I have outlined are intended to make clear that this government is prepared to take what steps are practical within our present tariff structure to reduce costs to Canadian users, to enable them to become more competitive, while keeping moderate protection where warranted.

There are, of course, a number of other tariff changes proposed of a relatively minor character. Some of them will reduce costs for certain industries, others are simply of a technical character intended to keep our tariff structure and language up-to-date. Details of all of these changes are set out in the Ways and Means Motion which I will be tabling.

I should like to refer to one further change in the tax legislation. This is a change to ensure that the withholding tax of 15 per cent is, in fact, applied on income received by non-residents on their investments in certain forms of commercial paper issued by Canadian debtors. This measure will help in effecting the adjustment of the capital flows in our balance of payments, a problem to which I referred earlier.

Let me now acquaint the House with our latest estimates of the revenues, expenditures and cash requirements of the government for the current fiscal year. I should refer briefly to the fiscal year 1970-71 first. The budgetary deficit for that year was just short of \$420 million which represents a swing of \$810 million from the surplus of approximately \$390 million in the previous year. On the non-budgetary side, the increase in cash requirements was rather more than \$550 million, making a total increase in requirements last fiscal year compared with the previous year of more than \$1,360 million. This is apart from funds required to finance exchange transactions. Whether certain payments will fall into one fiscal year or the next is always subject to some uncertainty as the calendar is rigid, but the progress of payments in relation to on-going and expanding programs is less rigid. The increase in our total cash requirements was some \$500 million less than I indicated in my budget of last December because of such factors. In respect of some categories of spending these differences were fairly large, but there were offsetting changes in respect of others. The impact of the economic programs of the government upon the economy was not, however, materially affected by these rather technical matters of timing.

Some of these factors affect the forecast figures for the current fiscal year. In particular, they have served to make the non-budgetary cash requirements for the current fiscal year larger than I indicated last December. Taking account of the tax changes I have proposed tonight, I now anticipate that budgetary revenues in 1971-72 will be approximately \$13,660 million and that budgetary expenditures will be \$14,410 million. This implies a budgetary deficit of \$750 million. The net non-budgetary requirements apart from exchange fund transactions are expected to total \$1,680 million. The total cash requirements would thus be \$2,430 million, almost \$1,250 million higher than last fiscal year.

With the permission of the House, Mr. Speaker, I should like now for the information of members to include as an appendix to Hansard tables in the form normally provided with budget speeches. These include a summary statement of our cash requirements for 1970-71 and our current forecast for 1971-72, the yields for the same two years of our main categories of budgetary and old age security revenues and again for the same two years, tables and explanatory notes giving the budget figures in terms of the national economic accounts in the form published by the Bureau of Statistics together with a reconciliation with the budgetary accounts.

Pursuant to Standing Order 60 (1), I would also like to table the Notices of the Ways and Means Motions related to the tax reform and budgetary proposals I have outlined.

Mr. Speaker,

This brings me to the end of the budget speech, or should I say two budget speeches. Before I sit down I want to state, as simply as I can, where we are and where I think we're going.

I believe that the tax reform will give us a balanced and workable income tax system.

Starting from the premise that our society is undergoing profound change, the tax reform is a sensitive response to changing needs. It will enable us to raise in a much fairer way the taxes we need to make Canada function. It will be more equitable not only between the various sectors of our society but also within these groups. The load will be distributed more evenly and surely so that every person and every institution able to contribute will do so according to capacity.

The tax reform recognizes that we live in a private enterprise system in which effort and initiative must be rewarded if our society is to work effectively and efficiently. I believe that we have succeeded in striking a viable balance between equity and enterprise. This will enable us to get the savings and investment required for strong growth while ensuring that the less fortunate get a fair deal.

The tax reform recognizes that we live in a federal state and that the provinces must also obtain revenues from personal and corporation incomes. It has therefore been designed to permit and encourage the provinces to base their system upon it.

I believe that the tax reform will help create a mood and a setting in Canada in which we may with greater certainty and confidence proceed to solve our national problems through the decade of the seventies and beyond. I am hopeful also that it will make an early and telling contribution to the pressing problems of this year and next.

As to the problems of right now it is evident that unemployment is too high. There is too much slack in the economy. At the same time costs are still rising at a rate that causes concern about future price developments. It is evident also that these problems are interrelated. They must be treated and solved together.

I am sure that we turned the corner late last year, and despite some apparent hesitancy, are now clearly on the way up. I believe that the economy will gather strength and momentum as we move through the balance of this year and next. The tax reductions I have announced today will reinforce this upward trend and help speed us on our course.

I have no doubt that we will encounter squalls on the way, and experience moments of uncertainty. We will adjust as we have been adjusting, and as the facts warrant. But we will not be driven into irresponsible and ill-considered action.

We are on course. We shall most certainly succeed.

GOVERNMENT OF CANADA

BUDGETARY AND OLD AGE SECURITY REVENUES

(Millions of Dollars)

	<u>1970-71</u>	<u>1971-72</u>
	Preliminary	Forecast
		After Tax Changes

Budgetary Revenues

Personal Income Tax	5,263	5,960
Corporation Income Tax	2,217	2,000
Non-Resident Tax	258	280
Estate Tax	120	100
Custom Duties	814	840
Sales Tax	1,708	1,870
Other Duties and Taxes	964	1,020
 Total Taxes	11,344	12,070
Non-Tax Revenues	1,425	1,590
 Total Budgetary Revenues	12,769	13,660

Old Age Security Revenues

Personal Income Tax	1,132	1,270
Corporation Income Tax	208	170
Sales Tax	563	630
 Total Old Age Security Revenues	1,903	2,070

FEDERAL GOVERNMENT REVENUE AND EXPENDITURE ON
 A NATIONAL ACCOUNTS BASIS
 (Millions of Dollars)

	<u>1970-71</u>	<u>1971-72</u>
	Preliminary	Forecast
		After Tax Changes
<u>A - Revenue</u>		
Direct Taxes, Persons	7,535	8,485
Direct Taxes, Corporations	2,115	2,235
Direct Taxes, Non-Residents	260	280
Indirect Taxes	4,075	4,400
Other Current Transfers from Persons	5	5
Investment Income	1,250	1,375
Capital Consumption Allowances	235	270
 TOTAL REVENUE	 15,475	 17,050
<u>B - Expenditure</u>		
Current Goods & Services	4,540	5,030
(Non-Defence)	(2,675)	(3,160)
(Defence)	(1,865)	(1,870)
Transfer Payments to Persons	4,200	4,710
Subsidies	565	550
Capital Assistance	120	175
Current Transfers to Non-Residents	250	220
Interest on the Public Debt	1,880	2,030
Transfers to Provinces	3,675	4,225
Transfers to Local Governments	85	105
Gross Capital Formation	535	655
 TOTAL EXPENDITURE	 15,850	 17,700
 <u>C - Surplus (+) or Deficit (-)</u>	 - 375	 - 650

FEDERAL GOVERNMENT REVENUE

PUBLIC ACCOUNTS AND NATIONAL ACCOUNTS RECONCILIATION

(Millions of Dollars)

	<u>1970-71</u> Preliminary	<u>1971-72</u> Forecast After Tax Changes
1. Budgetary Revenue	12,769	13,660
<u>Deduct</u>		
2. Budgetary Return on Investment	- 989	- 1,045
3. Post Office Revenue	- 330	- 410
4. Other Non-Tax Budgetary Revenues	- 106	- 135
	(-1,425)	(- 1,590)
5. Corporate Income Tax, Excess of Accruals (+) over Collections (-)	- 310	65
<u>Add</u>		
6. Government Pensions and Social Security Receipts	2,883	3,145
Government Investment Income		
7. Interest on Loans, Advances and Investments	521	590
8. Interest Receipts on Social Insurance and Government Pension Funds	419	415
9. Profits before Taxes (net of losses) of Government business enterprises	310	370
	(1,250)	(1,375)
10. Capital Consumption Allowances	237	270
11. Miscellaneous ⁽¹⁾	71	125
12. Total Revenue, National Accounts Basis	15,475	17,050

(1) These miscellaneous adjustments represent insurance companies' tax revenues, miscellaneous indirect taxes, miscellaneous transfers from persons and adjustment for the supplementary period. In the national accounts, revenue in the supplementary period is shifted into the following fiscal year.

FEDERAL GOVERNMENT EXPENDITURE

PUBLIC ACCOUNTS AND NATIONAL ACCOUNTS RECONCILIATION

(Millions of Dollars)

	<u>1970-71</u> Preliminary	<u>1971-72</u> Forecast
1. Budgetary Expenditure	13,187	14,410
<u>Deduct</u>		
2. Budgetary Transfers to Funds and Agencies (1)	- 600	- 541
3. Post Office Expenditure	- 370	- 418
4. Deficit of Government Business Enterprises	- 84	- 87
5. Reserves and Write-offs	- 109	- 93
6. Purchase of Existing Capital Assets	- 7	- 7
7. Budgetary Revenue Items Offset against Budgetary Expenditure (2)	- 63	- 64
	(-1,233)	(-1,210)
<u>Add</u>		
8. Government Pensions and Social Security Benefits	2,875	3,315
9. Expenditure of Government Funds and Agencies (1)	666	627
10. Capital Consumption Allowances	237	270
11. Miscellaneous (3)	118	288
12. Total Expenditure, National Accounts Basis	15,850	17,700
13. Surplus (+) or Deficit (-), National Accounts Basis	- 375	- 650
14. Surplus (+) or Deficit (-), Budgetary Basis	- 418	- 750

(1) In the National Accounts, budgetary appropriations to various funds and agencies are replaced by the expenditure actually made by these funds and agencies.

(2) This item mainly consists of revenue from sales of goods and services by the government. These sales appear as final expenditure of the private sector and are deducted to avoid double counting.

(3) This item includes the supplementary period adjustment. In the National Accounts, expenditures on goods and services in the supplementary period are divided between adjacent fiscal years; most other expenditures are shifted entirely to the next fiscal year.

GOVERNMENT OF CANADA FINANCIAL REQUIREMENTS

(Millions of Dollars)

	<u>1970-71</u>	<u>1971-72</u>
	Preliminary	Forecast
		After Tax Changes

Budgetary Transactions

Revenues.....	12,769	13,660
Expenditures.....	-13,187	-14,410
Surplus (+) or Deficit (-).....	- 418	- 750

Net Non-Budgetary Transactions (1)

Excluding foreign exchange transactions..-	764	- 1,680
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Total Government of Canada Financial Requirements

Excluding foreign exchange transactions..-	1,182	- 2,430
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<u>Amount Required to Date to Finance Foreign Exchange Transactions.....</u>	- 1,255	- 13 (2)
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Total Government of Canada Financial Requirements

Excluding future foreign exchange transactions.....	- 2,437	- 2,443
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(1) This item includes the changes in the non-marketable bonds held by the Unemployment Insurance Commission.

(2) As of May 31, 1971.

